

Message Text

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PAGE 01 LONDON 16068 01 OF 02 091817Z

51

ACTION EUR-12

INFO OCT-01 ISO-00 AEC-05 AID-05 CEA-01 CIAE-00 CIEP-01

COME-00 DODE-00 EB-07 FEAE-00 FPC-01 H-01 INR-05

INT-05 L-02 NSAE-00 NSC-05 OMB-01 PM-03 RSC-01 SAM-01

OES-03 SP-02 SS-15 STR-01 TRSE-00 FRB-01 NEA-06

OPIC-03 XMB-02 /090 W

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R 091807Z DEC 74

FM AMEMBASSY LONDON

TO SECSTATE WASHDC 6389

INFO AMEMBASSY OSLO

USMISSION OECD PARIS

LIMITED OFFICIAL USE SECTION 01 OF 02 LONDON 16068

E.O. 11652: N/A

TAGS: ENRG, UK

SUBJECT: HMG ANNOUNCES POLICIES ON OIL DEPLETION AND
REFINING

SUMMARY: ON DECEMBER 6 SECSTATE FOR ENERGY VARLEY OUT-LINED NEW HMG POLICIES ON DEPLETION OF NORTH SEA OIL RE-SERVES AND RELATED ONSHORE REFINING WHICH LARGELY ELIM-INATES FEARS THAT GOVERNMENT RESTRICTIONS IN THESE AREAS WOULD DISCOURAGE OR DELAY DEVELOPMENT. VARLEY'S STATE-MENT WAS CLEARLY MOTIVATED BY A DESIRE TO REMOVE A MAJOR ELEMENT OF UNCERTAINTY AND CONCERN IN OIL COMPANY CIRCLES STILL MUCH PREOCCUPIED BY PARTICIPATION NEGOTIATIONS AND NEW PETROLEUM REVENUE TAX. WHILE HMG IS TAKING POWERS TO CONTROL RATE OF OIL FIELD PRODUCTION AND SUPERVISE FUTURE REFINERY INVESTMENT, VARLEY STATEMENT UNDERLINES GOVERNMENT INTENTION TO ENCOURAGE RAPID AND UNFETTERED EXPLOITATION OF NORTH SEA AT LEAST UNTIL EARLY 1980'S.

END SUMMARY

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PAGE 02 LONDON 16068 01 OF 02 091817Z

1. ON DECEMBER 6 SECRETARY OF STATE FOR ENERGY ERIC VARLEY ANNOUNCED NEW HMG POLICIES ON DEPLETION OF NORTH SEA OIL RESERVES AND RELATED ONSHORE REFINING.

2. ON DEPLETION POLICY, VARLEY STATED: (A) INVESTMENT IN EXISTING FINDS OR IN ANY FUTURE DISCOVERIES BEFORE END OF 1975 WOULD BE PROTECTED BY A PROMISE THAT NO DELAY WOULD BE IMPOSED ON THEIR PRODUCTION PROGRAMS AND THAT NO CUT IN OUTPUT WOULD BE INTRODUCED UNTIL 1982 AT THE EARLIEST. (B) NO CUTS IN OUTPUT WOULD BE MADE ON ANY FIELD DISCOVERED UNDER EXISTING LICENSES UNTIL 150 PERCENT OF THE CAPITAL INVESTMENT HAD BEEN RECOVERED. (C) ANY CUTS THAT MIGHT BE IMPOSED IN THE FUTURE WOULD BE GENERALLY LIMITED TO 20 PERCENT, AT A MAXIMUM, AND WOULD ONLY BE CONSIDERED WITH DUE REGARD TO TECHNICAL AND COMMERCIAL ASPECTS OF OUTPUT AND NEEDS OF BRITISH INDUSTRY FOR A STEADY MARKET.

VARLEY ALSO PROMISED CONSULTATIONS WITH COMPANIES IF IT PROVED NECESSARY TO DELAY DEVELOPMENT OF FINDS MADE IN 1976 OR LATER SO THAT PREMATURE INVESTMENT WAS AVOIDED.

2. ON REFINING POLICY, VARLEY STATED THAT DEPARTMENT OF ENERGY IS TO TAKE POWERS TO GRANT OR REJECT INITIAL LICENSES FOR REFINERY APPLICATIONS ON THE BASIS OF UK NEEDS, BUT HE DID NOT SAY HMG CONTEMPLATED TAKING POWERS TO DIRECT FLOW OF OIL. INSTEAD, HE ASSUMED THAT UNDER NORMAL COMMERCIAL CIRCUMSTANCES ABOUT TWO-THIRDS OF CRUDE WILL BE PROCESSED IN UK WITH PROPORTION OF EXPORTS BRINGING ADDED BENEFITS TO UK BALANCE OF PAYMENTS. AT SAME TIME, VARLEY INDICATED GOVERNMENT WOULD SEEK TO INSURE EXISTING REFINERIES WERE UPGRADED TO PROCESS HEAVIER FRACTIONS OF BARREL INTO GASOLINE AND NAPHTHA THEREBY AVOIDING NEED FOR COSTLY IMPORTS AND PROVIDING GOOD BASE FOR EXPANDING PETROCHEMICAL INDUSTRY.

3. COMMENT: VARLEY'S DECLARATIONS ON OIL DEPLETION AND REFINING POLICY WERE CLEARLY MOTIVATED BY A DESIRE TO RE-

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PAGE 01 LONDON 16068 02 OF 02 091817Z

51

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LIMITED OFFICIAL USE SECTION 02 OF 02 LONDON 16068

MOVE A MAJOR ELEMENT OF UNCERTAINTY AND CONCERN IN OIL COMPANY CIRCLES STILL MUCH PREOCCUPIED BY NEGOTIATIONS OVER HMG PARTICIPATION AND NEW PETROLEUM REVENUE TAX (NOW TO BE ANNOUNCED EARLY IN THE NEW YEAR RATHER THAN IN SPRING BUDGET). WHILE GOVERNMENT IS TAKING POWERS TO CONTROL RATE OF PRODUCTION AND SUPERVISE FUTURE REFINERY CONSTRUCTION, VARLEY STATEMENT UNDERLINES INTENTION TO ENCOURAGE RAPID AND UNFETTERED EXPLOITATION OF NORTH SEA RESERVES AT LEAST UNTIL EARLY 1980'S WHEN TARGET OF 2 TO 2.8 M/B/D PRODUCTION HOPEFULLY WIIL BE REACHED.

4. INITIALLY FAVORABLE REACTION EXPRESSED IN PRIVATE CONVERSATION BY OIL COMPANY OFFICIALS AND CONSERVATIVE PARLIAMENTARY OPPOSITION TENDS TO CONFIRM OUR JUDGMENT THAT VARLEY ANNOUNCEMENT, PARTICULARLY AS REGARDS DEPLETION POLICY, IS MODERATE AND REASSURING STEP WHICH IN PRACTICE SHOULD HAVE BENEFICIAL EFFECT ON OVERALL CLIMATE OF OIL COMPANY - HMG RELATIONS ON NORTH SEA ISSUES. ALTHOUGH COMPANIES WOULD HAVE PREFERRED STILL GREATER

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PAGE 02 LONDON 16068 02 OF 02 091817Z

LEEWAY ON QUANTITY OF OIL WHICH COULD BE EXPORTED AND REFINED OUTSIDE BRITAIN, "UP TO TWO-THIRDS" REFINED IN UK REQUIREMENT IS NOT DEEMED UNREASONABLE. END COMMENT

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